BASIC WORLD TAX CODE

TITLE I
INCOME TAX

CHAPTER 1
GENERAL PROVISIONS

SEC. 1. TAX IMPOSED.

A tax is hereby imposed on the taxable income derived during the taxable year by any person.

SEC. 2. INCOME SUBJECT TO TAX.

(a) IN GENERAL. — Except as otherwise provided in this title —

(1) Every taxpayer shall pay tax on taxable income from sources within Progresa, and

(2) In addition, every resident taxpayer shall pay tax on investment and financial income from sources outside of Progresa.

(b) NONRESIDENTS AND SOURCES OF INCOME. — For tax treatment of nonresidents and for sources of income within and outside Progresa, see chapter 10.

SEC. 3. AMOUNT OF TAX.

(a) INDIVIDUALS. — In the case of an individual —

If the taxable income is —	The tax imposed by section I is —
Over 0 but not over PR 50,000	Zero
Over PR 50,000 but not over PR 100,000	15 percent of excess over PR 50,000
Over PR 100,000	PR 7,500 plus 30 percent of excess over PR 100,000

(b) ENTITIES. —

(1) IN GENERAL. — In the case of an entity, the tax imposed by section 1 is 30 percent of the taxable income.

(2) INSURANCE COMPANIES. — For special rules for insurance companies, see section 152.

SEC. 4. CREDITS.

Taxpayers shall be allowed the credits against the tax imposed by section 1 that are allowed by chapter 14.

SEC. 5. TREATMENT OF ESTATES.

(a) ESTATE TREATED AS INDIVIDUAL. — Except as provided in subsection (b), the estate of a deceased individual shall be treated as an individual.

(b) AMOUNT OF TAX. — In the case of a decedent who was a resident of Progresa at the time of death —

(1) in applying section 3(a) to the calendar year that includes the date of death, the income of the decedent and the income of the estate shall be treated as the income of one individual,

(2) the amount of tax on the taxable income of the estate for the next taxable year shall be determined under section 3(a), and

(3) the amount of such tax for all subsequent taxable years shall be 30 percent of taxable income.

CHAPTER 2
DEFINITIONS OF GENERAL APPLICATION

SEC. 11. DEFINITIONS APPLY TO ALL OF CODE.

Except as otherwise provided in this Code, the meaning given to any term by this chapter shall apply each place that term is used in this Code.

SEC. 12. TAXPAYER RELATED DEFINITIONS.

(a) PERSON. — The term "person" means any entity or individual.

(b) TAXPAYER. — The term "taxpayer" means any person subject to any tax imposed by this Code.

(c) ENTITY. — The term "entity" means —

(1) any corporation, cooperative, or other organization having legal status as a juridical person,

(2) any other organization carrying on a business (whether such business is carried on by the central government, a regional or local government, an agency of such a government, a religious, charitable, or other nonprofit organization, or otherwise), and

(3) in the case of a nonresident person, any permanent establishment in Progresa.

The term "entity" does not include a pass-through or a proprietorship.

(d) INDIVIDUAL. — The term "individual" means a physical person.

(e) PERMANENT ESTABLISHMENT. — The term "permanent establishment" means a fixed place of business in Progresa, or an agent resident in Progresa, through which the business of a nonresident person is carried on. To the extent provided in regulations, such term includes any other link or connection through which a nonresident person engages in economic activity in Progresa.

(f) PASS-THROUGH. — The term "pass-through" means a partnership or similar arrangement organized under the laws of Progresa that —

(1) is not a juridical person, corporation, cooperative, permanent establishment, proprietorship, or governmental or nonprofit organization,

(2) has 10 or fewer owners all of whom are resident individuals or their estates, and

(3) meets such standards for the proportional sharing by the owners of items of capital, income, and loss as may be prescribed by regulations.

(g) PROPRIETORSHIP. — The term "proprietorship" means a business owned 100 percent by one individual. For purposes of the preceding sentence, a husband and wife shall be treated as one individual if community property rules apply to their marriage.

(h) RESIDENT INDIVIDUAL. — Except as provided in regulations, the term "resident individual" means one who —

(1) has a principal place of abode in Progresa, or

(2) is physically present in Progresa on more than 182 days during the taxable year.

(i) RESIDENT ENTITY. — The term "resident entity" means an entity that is organized under the laws of Progresa. A permanent establishment shall be treated as a resident entity, but only with respect to its income sourced within Progresa.

(j) NONRESIDENT. — The term "nonresident" means not a resident of Progresa.

(k) FOREIGN. — The term "foreign" means sourced outside of Progresa.

(l) RELATED PERSON. —

(1) IN GENERAL. — Except as otherwise provided in regulations, the term "related person" means —

(A) a member of the taxpayer's family, and

(B) an entity or pass-through which controls, is controlled by, or is under common control with, the taxpayer.

(2) FAMILY MEMBER; CONTROL. — For purposes of paragraph (1) —

(A) The taxpayer's family includes the taxpayer's spouse, any ancestor or descendant of the taxpayer or the taxpayer's spouse, and the spouse of any ancestor or descendant of the taxpayer or spouse.

(B) The term "control" means the ownership (either directly or through one or more entities or pass-throughs) of 50 percent or more in value or voting power of the equity interests in the entity or pass-through being tested.

(C) For purposes of determining control, an individual shall be treated as owning all equity interests owned directly or indirectly by members of such individual's family.

SEC. 13. DEFINITIONS RELATED TO INCOME OR DEDUCTIONS.

(a) GROSS INCOME. — The term "gross income" means all gains and all other income from whatever source derived.

(b) SOME TYPES OF INCOME INCLUDED. — The term "gross income" includes (but is not limited to) —

(1) compensation for services, including wages, salaries, fees, commissions, and similar items,

(2) gross income derived from carrying on a business or a profession or similar activity,

(3) gain derived from transfers of rights in property (whether regular or occasional and whether connected with a business, an investment, or personal use),

(4) Interest (other than interest taxable under section 163),

(5) Rents,

(6) Royalties,

(7) Pensions and annuities, and

(8) Lottery and other gambling winnings.

(c) EXCLUSIONS FROM GROSS INCOME. — The term "gross income" does not include —

(1) mandatory employer contributions to government pension and welfare funds,

(2) gifts and inheritances, and distributions from estates,

(3) the proceeds of life insurance policies payable by reason of the death of the insured,

(4) indemnification for work accidents,

(5) compensation for sickness or injury payable pursuant to health or disability insurance,

(6) fringe benefits taxable under section 161,

(7) dividends excludable under section 164(e) or section 102(b).

(8) interest taxable under section 163,

(9) gain from the sale of a principal residence excluded under section 55,

(10) child support determined under decree or law,

(11) income of foreign diplomats and similar officials, to the extent provided in section 93, and

(12) all other items expressly excluded under this title.

(d) INCLUDIBLE INCOME. — The term "includible income" means the amount determined by excluding from gross income items —

(1) expressly excluded, or

(2) excluded by being sourced outside of Progresa under section 141.

(e) TAXABLE INCOME. — The term "taxable income" means includible income, reduced by the deductions.

(f) DEDUCTIONS. — The term "deductions" means the deductions allowable to the taxpayer under this title.

(g) NET. — The term "net" when used with respect to any category of income means the gross income from such category, reduced by the deductions attributable to such category.

SEC. 14. DIVIDEND AND SHAREHOLDER.

(a) DIVIDEND. — Except for stock dividends described in section 102(b) and distributions in complete liquidation described in section 103(b), the term "dividend" means any distribution by an entity to a shareholder in such entity with respect to the shareholder's equity interest in such entity. Whether or not a distribution is a dividend shall be determined under the preceding sentence without regard to whether or not the entity has earned profits during the current or prior years.

(b) SHAREHOLDER. — The term "shareholder" means any person owning an equity interest in an entity.

(c) ENTITIES OTHER THAN CORPORATIONS. — For purposes of this Code (but not for laws dealing with matters other than taxation) —

(1) any entity that is not a corporation shall be treated as if it were a corporation, and

(2) any person who holds an equity interest in (or may otherwise gain income or profit as a participant in) such an entity shall be treated as a shareholder of such entity.

SEC. 15. BUSINESS.

The term "business" includes any trade. It also includes any rental or other activity entered into for profit where the taxpayer materially participates in the management of the activity on a regular, continuous, and substantial basis.

SEC. 16. INVESTMENT ACTIVITY.

The term "investment activity" means any activity entered into for profit where the taxpayer does not participate in the management of the activity on a regular, continuous, and substantial basis.

SEC. 17. EXECUTIVE POWER.

The term "Executive Power" means the President of Progresa.

SEC. 18. TAX ADMINISTRATOR.

The term "Tax Administrator" means the head of the Tax Service created by section 501.

SEC. 19. DESIGNATED OFFICER.

The term "designated officer" means, with respect to any function, the officer of the Tax Service designated in accordance with law to carry out that function.

CHAPTER 3
DEDUCTIONS

SEC. 31. BUSINESS EXPENSES.

(a) ALLOWANCE OF DEDUCTION. — Subject to the provisions of this chapter, these shall be allowed as a deduction from includible income the expenses paid or incurred by the taxpayer during the taxable year to carry on a business.

(b) BUSINESS EXPENSES OF EMPLOYEES AND SELF-EMPLOYED INDIVIDUALS. —

(1) IN GENERAL. — If the taxpayer's business is the performance of services as an employee, or if the taxpayer is a self-employed individual, subsection (a) shall apply to travel, meals and lodging, moving expenses, and similar items only to the extent, and under the circumstances, prescribed in regulations.

(2) MINIMUM THRESHOLD. — The first PR 1,000 of business expenses of an employee or self-employed individual for the taxable year may not be deducted.

(c) LIMITATION WHERE EXPENSE HAS MIXED ELEMENTS. — In any case where an expense would (but for this subsection) meet the requirements of subsection (a) but has an element other than the business element, a deduction shall be allowable —

(1) only if the business element predominates, and

(2) only for that portion of the expense directly related to the business element.

SEC. 32. ITEMS NOT DEDUCTIBLE.

(a) CAPITAL EXPENDITURES. — Except as provided in paragraph (1) of section 36, amounts paid for new buildings or for permanent improvements or betterments made to increase the value of any property (including any construction period interest and taxes), instead of being allowed as an immediate deduction, shall be placed in a capital account. To the extent and in the manner provided in this title or in regulations, the balance in such account shall be allowed over time as a deduction for depreciation, amortization, or depletion.

(b) AMUSEMENT, ENTERTAINMENT, AND SIMILAR EXPENSES. — No deduction shall be allowed under this title for any expense for an activity generally considered to be amusement, entertainment, or recreation, or for the use of any facility in connection with such an activity. This subsection shall not apply to expenses incurred by the taxpayer in connection with the taxpayer's business of furnishing amusement, entertainment, or recreation.

(c) PERSONAL, LIVING, AND FAMILY EXPENSES. — Except as otherwise expressly provided in this title, no deduction shall be allowed under this title for personal, living, or family expenses.

(d) TAXES. — No deduction shall be allowed under this title for any tax imposed by section 1 (income tax) or any other provision of this title (other than section 161, the fringe benefit tax).

(e) PAYMENTS TO RELATED PERSONS. — No deduction shall be allowed under this title for any compensation or emoluments paid to an officer or director of an entity, to a partner or other member of a pass-through, or to any member of the taxpayer's family or other related person (as defined in section 12(l)) unless there is proof that the payment is for services actually performed, and then only to the extent the amount of the compensation and emoluments is reasonable. A similar rule shall apply in the case of interest, rent, and other expenses.

(f) LOSS ON SALE TO RELATED PERSON. — No deduction shall be allowed in respect of any loss from the sale or exchange of property, directly or indirectly, between related persons (as defined in section 12(l)).

(g) EXEMPT INCOME. — No deduction shall be allowed under this title to acquire, manage, or conserve any property the income from which is exempt from tax under this title or is subject to a reduced rate of tax under section 163.

(h) NONDOCUMENTED EXPENSES. — No deduction shall be allowed under this title for any expense unless the taxpayer establishes, in the manner required by regulations, that such expense was incurred, the purpose therefor, and the amount thereof.

SEC. 33. INTEREST. —

(a) ALLOWANCE OF DEDUCTION. — There shall be allowed as a deduction interest paid or incurred by the taxpayer during the taxable year in carrying on a business.

(b) LIMITATION ON DEDUCTION BY CERTAIN ENTITIES. — In the case of an entity described in subsection (c), the maximum amount that may be deducted under this title for interest for any taxable year is an amount equal to the sum of —

(1) the taxpayer's interest income, plus

(2) 50 percent of the taxpayer's net noninterest income.

(c) ENTITIES OWNED BY NONRESIDENTS OR TAX EXEMPT ORGANIZATIONS. — For purposes of subsection (b), an entity is described in this subsection if 50 percent or more in value of the equity interests in such entity are owned (directly or indirectly) by nonresident persons or by an organization exempt from tax under section 91.

(d) MEANING OF TERMS. — For purposes of subsection (b) —

(1) the term "net noninterest income" means includible income (other than interest income), reduced by the deductions other than the deduction for interest, and

(2) interest income and net noninterest income shall be determined by taking into account only items which relate to carrying on the taxpayer's business for the taxable year.

(e) CARRYFORWARD OF DISALLOWED INTEREST. — Any interest which qualifies under subsection (a) for the taxable year but which is not allowed for that year because of subsection (b) shall be treated as qualifying under subsection (a) for the next taxable year.

SEC. 34. DEPRECIATION.

(a) DEPRECIABLE PROPERTY DEFINED. — For purposes of this title, the term "depreciable property" means property used in the business of a kind which is likely to lose value because of wear and tear or obsolescence.

(b) DETERMINATION OF DEDUCTION. — The allowance for depreciation (or amortization) of depreciable property shall be determined under this section and sections 35 and 36.

(c) AMOUNT ALLOWED. — The amount allowed as a depreciation deduction for the taxable year for any category of property shall be determined by applying to the capital account (at the close of the taxable year) for such category the applicable percentage under subsection (f).

(d) THREE CATEGORIES OF TANGIBLE DEPRECIABLE PROPERTY. — All depreciable property of the taxpayer other than intangibles shall be placed in one of the following three categories:

(1) CATEGORY 1. — Buildings and their structural components.

(2) CATEGORY 2. — Automobiles and light general duty trucks; office furniture and equipment; and computers, information systems, and data handling equipment.

(3) CATEGORY 3. — All other tangible property.

(e) TREATMENT OF CATEGORIES. —

(1) CATEGORY 1. — Property in Category 1 shall be accounted for on a segregated asset account basis.

(2) CATEGORY 2. — All Category 2 property of the taxpayer shall be placed in one pool.

(3) CATEGORY 3. — All Category 3 property of the taxpayer shall be placed in one pool.

(f) APPLICABLE PERCENTAGES. — The applicable percentages for Categories 1, 2, and 3 shall be determined in accordance with the following table:

Category	Applicable Percentage
1	5
2	25
3	15

(g) ADDITIONS TO ACCOUNT. — The initial addition to capital account for any acquired property shall be its cost (plus insurance and freight). The initial addition to capital account for any self-constructed property shall include all taxes, duties, and interest attributable to such property for periods before the property is placed in service.

(h) WHEN ASSETS TAKEN INTO ACCOUNT. — An asset shall first be taken into account for purposes of this section when it is placed in service.

(i) STARTING AMOUNT FOR PRE-1996 DEPRECIABLE AND DEPLETABLE PROPERTY. — The starting amount for any depreciable or depletable property held by the taxpayer on January 1, 1996, shall be its

adjusted basis at the beginning of such day. For this purpose, the allowance for depreciation, the allowance for depletion, and all other adjustments for prior periods shall be made under applicable prior income tax laws.

(j) DEPRECIATION OF INTANGIBLES. — The depreciation of each intangible (including patents, copyrights, drawings, models, contracts, and franchises) having a limited life shall reflect the life of the property and the straight line method of depreciation.

SEC. 35. POOLED ASSET ACCOUNTS.

(a) APPLICATION OF SECTION. — This section shall apply to the pools for Category 2 and 3 property.

(b) ONE-HALF YEAR CONVENTION FOR ADDITIONS. — If during the taxable year property is added to a pool referred to in subsection (a), then one-half of the addition shall be taken into account for the year the property is so added and one-half for the next year.

(c) DISPOSITIONS. — If during the taxable year property in a pool referred to in subsection (a) is disposed of, the capital account shall be reduced by any amount realized from such disposition. One-half of the reduction shall be taken into account for the year the property is disposed of and one-half for the next year. If the disposition results in a negative balance in the pool, an amount equal to such negative balance shall be included in income (and the pool balance shall be restored to zero).

(d) TERMINATION OF POOLS. — When at the close of the taxable year a pool no longer contains any property, then any balance in the pool shall be deductible as a loss.

SEC. 36. REPAIRS AND IMPROVEMENTS.

In the case of any segregated asset account described in section 34 and any pooled asset account described in section 35 —

(1) to the extent the amounts expended during the taxable year to repair, maintain, or improve the property do not exceed 5 percent of the balance in the account at the beginning of the year (before adjustments for additions and dispositions), such amounts shall be allowed as a deduction for such year, and

(2) to the extent such amounts exceed 5 percent, such excess shall be treated as improvements and added to the segregated asset or pooled account.

SEC. 37. DEPLETION.

(a) DETERMINATION OF DEDUCTION. — In the case of any natural deposit (including any oil or gas well) the allowance under section 31(a) for depleting that deposit shall be determined under this section.

(b) COSTS TO BE CAPITALIZED. — All exploration and development costs (and interest attributable thereto) shall be added to the capital account of the deposit.

(c) UNIT OF PRODUCTION ALLOWANCE. — The amount allowed as a depletion deduction with respect to any deposit for the taxable

year shall be determined by multiplying the balance in the capital account for the deposit by a fraction —

(1) the numerator of which is the units produced from the deposit during the year, and

(2) the denominator of which is the estimated total production from the deposit (determined at the time and in the manner provided by regulations).

SEC. 38. CHARITABLE CONTRIBUTIONS.

(a) ALLOWANCE OF DEDUCTION. — There shall be allowed as a deduction any charitable contribution made by the taxpayer during the taxable year that falls within the allowable amount set forth in subsection (b).

(b) 5-PERCENT ALLOWABLE AMOUNT. — The amount allowable under this section for any taxable year shall be so much of the aggregate charitable contributions of the taxpayer for the taxable year —

(1) as exceeds 2 percent of the taxpayer's taxable income, but

(2) does not exceed 7 percent of the taxpayer's taxable income.

For purposes of the preceding sentence, the taxpayer's taxable income shall be determined before any deduction under this section.

(c) CHARITABLE CONTRIBUTIONS DEFINED. — For purposes of this section, the term "charitable contribution" means a contribution

or gift to or for the use of an organization described in paragraph (1) or (2) of section 91(b).

(d) VERIFICATION. — A contribution or gift shall be allowable as a deduction only if verified in the manner required by regulations.

SEC. 39. BUSINESS LOSS CARRYFORWARD.

(a) LOSS CARRYFORWARD. — If the taxpayer's business deductions for the taxable year exceed the taxpayer's business includible income for such year, the amount of such loss shall be a carryforward to each of the 5 succeeding taxable years and available as a deduction against any business includible income arising in such succeeding years.

(b) AMOUNT ALLOWED IN LATER YEARS. — The amount of the carryforward taken into account for any taxable year after the year of the loss shall be the entire amount of the loss, reduced by the aggregate amount allowed as a deduction under this section for the intervening years.

(c) MORE THAN ONE BUSINESS LOSS. — If the taxpayer has a business loss described in subsection (a) in more than one year, this section shall be applied to the losses in the order in which they arose.

SEC. 40. TREATMENT OF INVESTMENT EXPENSES.

(a) GENERAL RULE. — The operational expenses of carrying on an investment activity shall be allowed as a deduction from the operational income of such activity for such year, but only to the extent such expenses do not exceed such income. For purposes of the preceding

sentence, the first PR 1,000 of expenses for the taxable year shall be disregarded.

(b) DETERMINATION OF OPERATIONAL INCOME AND EXPENSE. — For purposes of subsection (a), the amount of the operational income and expenses of any investment activity shall be determined under this chapter as if the investment activity constituted a business, with the following modifications —

(1) gains and losses from the sale, exchange, or disposition of investment assets shall not be taken into account under this section but shall be taken into account as provided in sections 52 and 53, and

(2) the deduction under section 38 for charitable contributions shall not be allowed.

(c) INVESTMENT OPERATIONAL LOSS CARRYFORWARD. — If for any taxable year the operational expenses for an investment activity exceed the taxpayer's operational income from such activity for the year, the amount of such loss shall be an operational loss carryforward to each of the 5 succeeding taxable years and available as a deduction to offset any operational income from such activity for such succeeding years. The amount of the carryforward for any taxable year after the year of the loss shall be the entire amount of the loss, reduced by the aggregate amount allowed under this subsection for the intervening years. If the taxpayer has an operational loss in more than one year, this subsection shall be applied to the losses in the order in which they arose.

CHAPTER 4
GAINS AND LOSSES AND RELATED MATTERS

SEC. 51. DEFINITIONS RELATED TO ASSETS.

(a) BASIS. — For purposes of this Code —

(1) PURCHASED OR CONSTRUCTED ASSETS. — The term "basis", when applied to an asset purchased or constructed by the taxpayer, means the asset's cost.

(2) EXPRESSLY PROVIDED BASIS. — Whenever a provision of this Code expressly provides the basis for an asset, the term "basis" means the amount so provided.

(3) OTHER ASSETS. — In the case of an asset not described in paragraph (1) or (2), the term "basis" means whichever of the following is appropriate —

(A) the adjusted basis of the person who transferred the asset to the taxpayer, or

(B) the adjusted basis of the old asset exchanged for the asset in question.

In any case to which this paragraph applies, the basis shall be appropriately increased (or reduced) for additional consideration furnished by (or received by) the taxpayer.

(b) ADJUSTED BASIS. — For purposes of this Code, the term "adjusted basis" means the basis —

(1) reduced by depreciation, depletion, and other items of reduction properly chargeable to capital account, and

(2) increased by the cost of improvements (not including items deductible under section 36) and other items of addition properly added to capital account.

Adjustments for periods before January 1, 1996, shall be made under applicable prior income tax laws.

(c) CAPITAL ACCOUNT. — For purposes of this Code, the term "capital account" means the account established for an asset (or pool of assets) on the books of the taxpayer.

(d) BUSINESS AND NONBUSINESS ASSETS. — For purposes of this Code —

(1) BUSINESS ASSET. — The term "business asset" means any asset (other than land and securities) used in the business.

(2) NONBUSINESS ASSET. — The term "nonbusiness asset" means any asset that is not a business asset.

(3) INVESTMENT ASSET. — The term "investment asset" means any security, land, or other asset that is a nonbusiness asset held for profit.

(4) PERSONAL ASSET. — The term "personal asset" means any nonbusiness asset that is not an investment asset.

SEC. 52. RECOGNITION AND AMOUNT OF GAIN OR LOSS.

(a) RECOGNITION OF GAIN OR LOSS. — Except as otherwise provided in this title, the entire amount of the gain or loss on the sale, exchange, or other disposition of property shall be recognized.

(b) AMOUNT REALIZED. — The amount realized from the sale, exchange, or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. Such term includes the amount of any indebtedness of the transferor with respect to the transferred property that is assumed or forgiven in connection with the transfer.

(c) AMOUNT OF GAIN. — The gain from the sale, exchange, or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis of the property.

(d) AMOUNT OF LOSS. — The amount of the loss from the sale, exchange, or other disposition of property shall be the excess of the adjusted basis over the amount realized.

SEC. 53. LIMITATIONS ON RECOGNITION OF NONBUSINESS LOSSES.

(a) LOSSES ON SECURITIES. —

(1) LIMIT. — In the case of any taxpayer (whether an individual or an entity) losses for the taxable year on the disposition of securities that are investment assets shall be allowed only to the extent of gains for such year on the disposition of such securities.

(2) CARRYFORWARD. — Any loss disallowed for the taxable year by reason of paragraph (1) shall be treated as a securities loss realized in the next year.

(3) YEAR OF DEATH. — Paragraph (1) shall not apply with respect to an individual for the taxable year in which the individual dies.

(b) LOSSES ON PERSONAL ASSETS. — No deduction shall be allowed on the disposition of any personal asset.

(c) GAMBLING LOSSES. — Gambling losses shall be allowed as a deduction, but only to the extent of gambling gains for the same taxable year.

SEC. 54. PROPERTY TRANSFERS BETWEEN SPOUSES.

No gain or loss shall be recognized on —

(1) any transfer of property between spouses, or

(2) any transfer of property between former spouses, but only if such transfer is part of an overall property settlement incident to the divorce.

The basis of the transferee in any property to which the preceding sentence applies shall be the adjusted basis of the transferor.

SEC. 55. EXCLUSION OF GAIN ON SALE OF PRINCIPAL RESIDENCE.

(a) EXCLUSION. — Gross income does not include gain from the sale, exchange, or other disposition of the taxpayer's principal residence.

(b) LIMITATION. — The amount of gain excluded under subsection (a) with respect to any residence shall not exceed PR 500,000. If the sales price of the residence exceeds PR 500,000, the amount of gain excluded shall not exceed the portion of the gain that bears the same ratio to PR 500,000 as PR 500,000 bears to the sale price of the residence.

(c) PRINCIPAL RESIDENCE DEFINED. — To be treated as the taxpayer's principal residence for purposes of this section, the residence must have been owned by the taxpayer throughout the 3-year period ending on the date of the disposition, and it must have been the taxpayer's principal residence throughout that period.

SEC. 56. GIFTS.

(a) IN GENERAL. — The donor of any gift (including gifts to organizations referred to in section 91(b)) shall be treated as having sold the gift property at the higher of —

(1) its adjusted basis, or

(2) its fair market value on the date of the gift.

(b) BASIS. — The basis of the donee of a gift shall be the amount determined under subsection (a).

SEC. 57. PROPERTY PASSING AT DEATH.

(a) RECOGNITION OF GAIN. — Except as provided in subsection (d), the decedent shall be treated as having sold on the date of death (at its then fair market value) all property (other than exempt property) that passes by reason of his or her death.

(b) BASIS. — In the hands of the estate or successors to the deceased —

(1) IN GENERAL. — The basis of property treated as sold by reason of subsection (a) shall be the value taken into account under subsection (a), and

(2) EXEMPT PROPERTY. — The basis of exempt property shall be its adjusted basis in the hands of the decedent.

(c) EXEMPT PROPERTY. — For purposes of this section, the term "exempt property" means —

(1) the principal residence of the deceased,

(2) tangible personal property which was neither business property nor investment property in the hands of the deceased, and

(3) pensions, annuities, and other properties and rights which will yield periodic payments that are properly taxable to the successors as income that would have been includible income to the decedent if he or she had lived.

(d) CARRYOVER BASIS FOR CONTROLLING INTEREST IN SMALL BUSINESS. —

(1) IN GENERAL. — If by reason of the death of the decedent the controlling interest in a small business passes to members of the decedent's immediate family, such members may elect (in lieu of the immediate recognition of gain provided by subsection (a)) to have their respective bases in such controlling interest determined by reference to the decedent's adjusted basis for such controlling interest.

(2) DEFINITIONS. — For purposes of paragraph (1) —

(A) SMALL BUSINESS. — The term "small business" means an active business having a net worth (on the date of the decedent's death) of not more than PR 10,000,000.

(B) IMMEDIATE FAMILY. — The term "immediate family" means the spouse, children, and such other close relatives of the deceased as may be specified in regulations.

(C) CONTROLLING INTEREST. — The term "controlling interest" means the ownership of 50 percent or more in value of the equity in a proprietorship, pass-through, or entity.

(3) LIMITATION TO ONE SMALL BUSINESS. — If at the time of death the decedent owned a controlling interest in more than one small business, this subsection shall

apply only to the one small business selected by the members of the decedent's immediate family.

(e) REGULATIONS. — The Tax Administrator shall prescribe such regulations as may be necessary or appropriate to carry out this section.

SEC. 58. NONRECOGNITION OF GAIN ON INVOLUNTARY CONVERSIONS.

(a) NONRECOGNITION. — Gain shall not be recognized on the involuntary conversion of property to the extent that the consideration received by reason of the conversion consists of —

(1) like kind property, or

(2) money that is reinvested in like kind property within the replacement period.

(b) BASIS. — In any case where there is nonrecognition of gain by reason of subsection (a), the basis of the replacement property shall be determined by reference to the adjusted basis of the old property.

(c) DEFINITIONS. — For purposes of this section —

(1) INVOLUNTARY CONVERSION. — Property is involuntarily converted if in whole or in part the property is destroyed, stolen, seized, or condemned, or the taxpayer is otherwise forced to dispose of the property by reason of threat or imminence of any of the foregoing.

(2) LIKE KIND PROPERTY. — Replacement property shall be considered like kind property if it is of the same

character or nature (whether or not it is of the same grade or quality).

(3) REPLACEMENT PERIOD. — The term "replacement period" means the period ending at the close of the second taxable year after the taxable year in which the conversion takes place.

SEC. 59. CERTAIN FOREIGN EXCHANGE TRANSACTIONS.

(a) DEBT DENOMINATED IN FOREIGN CURRENCY MARKED TO MARKET. — For purposes of this title, any debt —

(1) owed by or owed to the taxpayer, and

(2) the principal of which is denominated in a currency other than the Prog,

shall be treated as sold by the taxpayer on the last day of the taxable year at its then fair market value.

(b) EFFECT OF MARKING TO MARKET. — Any gain or loss resulting from the deemed sale under subsection (a) shall be treated as income or loss arising on the last day of the taxable year, and the basis of the debt in the hands of the taxpayer shall become such fair market value.

(c) OTHER FOREIGN CURRENCY TRANSACTIONS. — To the extent provided in regulations, subsections (a) and (b) shall be extended to transactions involving an obligation to pay in a currency other than the Prog in the case of —

(1) items of expense or of gross income or receipts where the items are to be paid or received after accrual, and

(2) forward contracts, futures contracts, options, and similar financial instruments.

SEC. 60. LOSSES ON CERTAIN SALES OF STOCK AND SECURITIES.

(a) GENERAL RULE. — Where within 30 days before or 30 days after the date of the disposition of stock or securities the taxpayer acquires substantially identical property —

(1) loss on such disposition shall not be recognized, and

(2) the basis of the acquired property shall be the basis of the disposed of stock or securities, increased or decreased (whichever is appropriate) by the difference in the acquisition prices of the two properties.

(b) EXTENSION TO SHORT SALES. — Subsection (a) shall be extended by regulations to cases involving short sales of substantially identical stock or securities within 30 days before or 30 days after the date the short sale is closed.

CHAPTER 5
ACCOUNTING PROVISIONS

SEC. 71. TAXABLE YEAR.

The taxable year of each taxpayer shall be the calendar year.

SEC. 72. METHOD OF ACCOUNTING.

(a) IN GENERAL. — Except as otherwise provided in this section —

(1) an individual may use the cash or accrual method of accounting, and

(2) an entity or pass-through shall use the accrual method of accounting.

(b) MUST REFLECT INCOME. — The method of accounting used by the taxpayer must clearly reflect the taxpayer's income.

(c) CERTAIN LARGE BUSINESSES. — The designated officer may require an individual who is operating a large business to use the accrual method with respect to that business when the use of that method is necessary to clearly reflect the income of the business. The size and the circumstances of a large business to which this subsection applies shall be determined under regulations of general application.

(d) TAXPAYER MAY CHANGE METHOD WITH APPROVAL. — With the approval of the designated officer, the taxpayer may change a method of accounting to another method.

(e) CHANGE IN METHOD OF ACCOUNTING. — If the taxpayer's method of accounting is changed, adjustments in items of income,

deduction, credits, and other items shall be made so that no item is omitted and no item is included more than once.

SEC. 73. CASH AND ACCRUAL METHODS OF ACCOUNTING.

(a) CASH METHOD. — For purposes of this title, the cash method is the method under which in general —

(1) income is reported for the year when it is actually or constructively received in cash (or its equivalent) or in other property, and

(2) deductions are taken for the year in which the expenses or other items are actually paid,

unless they should be taken into account for a different period to clearly reflect income (as in the case of prepaid expenses or depreciation allowances).

(b) ACCRUAL METHOD. — For purposes of this title, the accrual method is a method under which in general —

(1) income is reported for the year in which it is earned or actually or constructively received, and

(2) deductions are taken for the year in which the expenses or other items are accrued or sustained

unless they should be taken into account for a different period to clearly reflect income.

(c) TESTS FOR ACCRUAL DEDUCTIONS. — Except as otherwise provided in regulations, an accrual method taxpayer may deduct an expense or other item only for the first year by the end of which all 3 of the following tests have been met —

(1) all facts determining the taxpayer's liability have occurred,

(2) economic performance with respect to the item has occurred, and

(3) the amount of the taxpayer's liability can be readily determined.

(d) ACCRUAL OF DEDUCTIONS BETWEEN RELATED PERSONS. — In the case of a taxpayer who uses the accrual method of accounting, no deduction shall be allowed before payment if the expense or other item involves an obligation to a related person who uses the cash method of accounting.

SEC. 74. INVENTORIES.

(a) WHEN TAXPAYER MUST ESTABLISH INVENTORIES. — Any person who maintains stocks of goods in process or of finished goods shall, if necessary to clearly reflect income, establish and maintain inventories of such stocks.

(b) INVENTORY METHOD. — The inventory method used by the taxpayer shall be LIFO (last-in, first-out) or such other method as may be permitted by regulations.

SEC. 75. LONG-TERM CONTRACTS.

(a) PERCENTAGE OF COMPLETION METHOD USED. — The income, deductions, and all other items with respect to a long-term contract shall be taken into account under the percentage of completion method. On completion of any long-term contract the taxpayer shall pay (or shall be entitled to receive) interest determined by applying the look-back method of subsection (b)(2) with respect to the contract.

(b) PERCENTAGE OF COMPLETION METHOD. —

(1) IN GENERAL. — All items of income and cost and all other items shall be allocated (in the manner provided in regulations) to a taxable year in the contract period on the basis of estimates of the percentage of the total work under the contract performed during such year. The returns for such years (except the year of completion) shall be filed using such estimates (or amendments thereto) approved by the designated officer.

(2) LOOK-BACK METHOD. — On the completion of the contract, solely for purposes of determining interest, the allocation to each taxable year on a percentage of completion basis shall be redetermined using the actual items rather than the estimated items. The interest on any underpayments or overpayments of any year resulting from such redetermination shall be determined under section 561 and shall be due and payable on the due date for the return of the taxable year in which the contract is com-

pleted. Also, the period of limitations for applying this section to any long-term contract shall begin from the date of furnishing the return for the year in which the contract was completed, rather than from any earlier date.

(c) LONG-TERM CONTRACT. — For purposes of this title, except as provided in regulations, the term "long-term contract" means any contract for the manufacture, building, installation, or construction of property if such contract is not completed within 18 months after the date on which such contract is entered into.

SEC. 76. ORIGINAL ISSUE DISCOUNT.

(a) CURRENT INCLUSION. — There shall be included in the gross income of the holder of any debt instrument having original issue discount an amount equal to the sum of the daily portions of the original issue discount for each day during the taxable year on which such holder held such debt instrument.

(b) ORIGINAL ISSUE DISCOUNT DEFINED. — For purposes of this section, the term "original issue discount" means the amount by which —

(1) the price at which the debt is to be redeemed at maturity, exceeds

(2) the price at which the instrument was issued.

(c) REGULATIONS. — The Tax Administrator shall prescribe such regulations as may be necessary or appropriate to carry out this section, including regulations for determining —

(1) the debt instruments to which this section applies,

(2) the amount of the original issue discount (whether the instrument is issued for money or other property), and

(3) the portion of the original issue discount allocable to each day.

SEC. 77. INCOME FROM JOINT PROPERTY.

Income derived from jointly held property shall be treated as derived by the owners in proportion to their respective interests in the property.

SEC. 78. ALLOCATION OF INCOME AND DEDUCTIONS AMONG TAXPAYERS.

(a) GENERAL RULE. — In the case of two or more entities or businesses (whether or not incorporated and whether or not organized in Progresa), under common ownership, the designated officer may distribute, apportion, or allocate gross income, deductions, credits, or allowances between or among such entities or businesses and their owners if the designated officer determines that such distribution, apportionment, or allocation is necessary in order to prevent evasion of taxes or clearly to reflect the income of any such entity, business, or owner.

(b) COMMON OWNERSHIP. — For purposes of subsection (a), two or more entities or businesses are under common ownership if the same persons own (directly or indirectly) 50 percent or more in value of the equity interests in each such entity or business.

SEC. 79. ADJUSTMENTS FOR INFLATION.

(a) DETERMINATION OF INFLATION PERCENTAGE. — If during any calendar year there is an increase of 5 percent or more in the Designated Price Index, the Tax Administrator shall determine and publish the inflation percentage for such year (in this section called the "adjustment year").

(b) APPLICATION OF INFLATION PERCENTAGE. — The inflation percentage described in subsection (a) shall be applied to the adjustment year as either —

(1) a bracket adjustment, or

(2) a comprehensive adjustment.

The selection of the type of adjustment shall be made by the Tax Administrator after weighing the severity of the inflation against the compliance and administrative costs of implementing a comprehensive adjustment.

(c) BRACKET ADJUSTMENT. — In a bracket adjustment the inflation adjustment shall be applied only to —

(1) the brackets set forth in sections 3 and 171 (wage withholding), and

(2) any other amount in this Code expressed in terms of "PR."

(d) COMPREHENSIVE ADJUSTMENT. — In a comprehensive adjustment the inflation percentage shall be applied to —

(1) the brackets and amounts described in subsection (c),

(2) the equity-financed portion of business assets and investment assets,

(3) carryforwards, underpayments, and overpayments from prior periods, and

(4) to the extent provided in regulations, any other matter that affects the determination of taxable income or the payment of tax (including withheld tax and advance payments).

(e) DESIGNATED PRICE INDEX. — For purposes of this section, the term "Designated Price Index" means the price index (whether of consumer prices, producer prices, or otherwise) maintained by the Central Bank that the Tax Administrator determines is most appropriate to mitigate the effects of inflation on the tax system.

(f) SHORTER ADJUSTMENT PERIODS. — Where the inflation rate substantially exceeds a 5 percent annualized rate, the Tax Administrator may provide for the application of this section on the basis of adjustment periods consisting of months, quarters, or other periods shorter than one year.

(g) APPLICATION OF SUBSECTION (d)(2) TO A BUSINESS. — Subsection (d)(2) shall be applied to a business by taking the following steps:

(1) determine the net equity ratio — that is, the relationship of —

(A) the total assets of the business, reduced by the total debt of the business, to

(B) the total assets of the business, and

(2) apply the product of the net equity ratio and the inflation adjustment to each asset of the business (other than cash and accounts receivable).

For purposes of this subsection, the adjusted bases of assets shall be used, except that in the case of pooled assets, the balance in the pool shall be used.

(h) APPLICATION OF SUBSECTION (d)(2) TO INVESTMENTS. — Subsection (d)(2) shall be applied to the investment activities of the taxpayer by taking steps similar to those set forth in subsection (g).

(i) ASSETS AND LIABILITIES DENOMINATED IN FOREIGN CURRENCY. — Under regulations, assets and liabilities denominated in currencies other than the Prog shall not be taken into account in applying subsections (g) and (h).

(j) ROUNDING. — The regulations prescribed under this section shall include provisions for rounding amounts to the extent appropriate for efficient tax administration.

CHAPTER 6
EXEMPT INCOME; UNRELATED BUSINESS INCOME

SEC. 91. INCOME EXEMPT FROM TAX.

(a) IN GENERAL. — Except as otherwise provided by law, the income described in subsection (b) shall be exempt from tax under section 1.

(b) GOVERNMENTAL AND NONPROFIT INCOME. — The following income is referred to in subsection (a), but only to the extent such income is not taxable under section 92:

(1) the income of the central government, a regional or local government, or any agency of such a government,

(2) the income of any organization —

(A) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, and

(B) no part of the assets or earnings of which is used for the benefit of any private person, and

(3) the income of any labor organization, or any chamber of commerce, industry, or agriculture, no part of the net earnings of which is used for the benefit of any private shareholder or individual.

(c) LIST OF NONPROFIT ORGANIZATIONS. — The Tax Administrator shall prepare a list of the organizations that meet the requirements of paragraph (2) or (3) of subsection (b). Only organizations included

on such list shall be treated as exempt from tax by reason of such paragraph (2) or (3).

(d) APPEALS WITH RESPECT TO LIST. — For right of organization to appeal a refusal to list such organization under subsection (c) or a removal from list, see section 571.

(e) REGULATIONS. — The Tax Administrator shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations —

(1) providing for loss of tax exemption or other penalty where the organization (or persons associated with it) engages in self-dealing or any other transaction that interferes with, or might interfere with, the charitable or other purpose that is the basis for exemption under this section, and

(2) requiring annual returns of the types of organizations specified in the regulations.

SEC. 92. TREATMENT OF INCOME OF UNRELATED BUSINESS.

(a) BUSINESS TREATED AS SEPARATE TAXABLE ENTITY. — For purposes of this title, an unrelated business of an organization referred to in section 91(b) shall be treated as a separate entity taxable under section 1 on its unrelated business taxable income at the 30 percent rate set forth in section 3(b).

(b) UNRELATED BUSINESS. — For purposes of this title, the term "unrelated business" means any commercial or industrial business, or any other business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of the function or purpose constituting the basis for its exemption under section 91(b).

(c) UNRELATED BUSINESS TAXABLE INCOME. — For purposes of this title, the term "unrelated business taxable income" means the includible income derived by any organization from an unrelated business regularly carried on by it, reduced by the deductions allowed by chapter 3 which are directly related to the carrying on of such business.

SEC. 93. FOREIGN DIPLOMATIC AND CONSULAR INCOME.

(a) EXEMPTION. — The salary and other emoluments received by foreign diplomatic and consular representatives, officials, and employees in the exercise of their functions in Progresa shall be exempt from tax under this title.

(b) INTERNATIONAL ORGANIZATIONS. — The exemption granted by subsection (a) shall apply equally to the foreign representatives, officials, and employees of international organizations, and of the agencies of technical cooperation of other governments.

(c) EXEMPTION BASED ON RECIPROCITY. — Any exemption under this section shall be conditioned on the granting of reciprocal rights by the governments concerned.

CHAPTER 7
ENTITY ORGANIZATIONS, REORGANIZATIONS, LIQUIDATIONS, ETC.

SEC. 101. CONTRIBUTIONS TO CAPITAL.

The contribution of capital to an entity in exchange for an equity interest therein by a person or persons who (after the contribution) control the entity shall not be taxed under this title. In any such case, the basis of property in the hands of the entity shall be its adjusted basis in the hands of the person who contributed the property.

SEC. 102. DISTRIBUTIONS BY AN ENTITY.

(a) IN KIND DISTRIBUTIONS. — If any property (other than stock in the entity) is distributed by an entity to a shareholder with respect to the shareholder's equity interest (whether as a dividend, as a liquidating distribution, or otherwise), the entity shall recognize gain or loss as if such property had been sold to the distributee at its fair market value.

(b) STOCK DIVIDENDS. — Except as provided in regulations, gross income does not include any distribution of stock which does not in any way alter the respective equity interests in the entity of its shareholders.

(c) BASIS. — In any case to which subsection (b) applies, the basis of the taxpayer's old stock shall be allocated between the old stock and the new stock in proportion to their respective values.

SEC. 103. LIQUIDATIONS.

(a) PARTIAL LIQUIDATIONS. — Any partial liquidation of an entity shall be treated as a distribution for purposes of this title. For purposes of the preceding sentence, a redemption (other than a redemption in complete liquidation) shall be treated as a partial liquidation.

(b) COMPLETE LIQUIDATIONS. —

(1) IN GENERAL. — In the case of the complete liquidation of an entity —

(A) such entity shall take into account gain or loss as if it had sold the property distributed in the liquidation at its fair market value, and

(B) except as provided in paragraph (2), the recipients of the distributed property shall be treated as if they had exchanged their equity interest in the liquidated entity for an amount equal to the fair market value of such property.

(2) COMPLETE LIQUIDATION OF SUBSIDIARY. — In the case of the distribution of property of a subsidiary to a parent pursuant to the complete liquidation of the subsidiary, no gain or loss shall be recognized by the parent on the receipt of such property.

(3) MEANING OF TERMS. — For purposes of this subsection —

(A) COMPLETE LIQUIDATION. — The period during which the liquidation must be completed, and the other requirements for qualification as a complete liquidation, shall be established by regulations.

(B) SUBSIDIARY AND PARENT. — An entity shall be a subsidiary of a second entity (the "parent") if the second entity is in control (within the meaning of section 105(b)) of the first entity at all times during the liquidation period.

SEC. 104. QUALIFIED REORGANIZATIONS OF ENTITIES.

(a) TAX TREATMENT AT THE ENTITY LEVEL. — In the case of a qualified reorganization, except to the extent provided in regulations —

(1) the basis of the property held by the reorganized entity shall be determined by reference to the adjusted basis of such property immediately before the reorganization,

(2) transfers of business property among the parties to the reorganization shall be tax-free, but

(3) any consideration received by any person (including any party to the reorganization) which does not consist of an equity interest in a party to the reorganization shall be treated as a distribution to the recipient.

(b) EQUITY INTERESTS DISTRIBUTED TO SHAREHOLDERS. — If in any qualified reorganization an equity interest in a party to the reor-

ganization is distributed to any shareholder of a party to the reorganization, such distribution shall, except to the extent provided in regulations, be received by such shareholder tax-free.

(c) TREATMENT OF ITEMS OF OLD ENTITY. — In the case of a qualified reorganization, except to the extent provided in regulations, the acquiring entity shall succeed to and take into account the method of accounting of the acquired entity, together with its inventories, loss carryforwards, credit carryforwards, dividend account, and all other items in such a manner that the acquiring entity takes the place of the acquired entity with respect to such items.

SEC. 105. DEFINITIONS AND RULES RELATING TO REORGANIZATIONS OF ENTITIES.

(a) ENTITY REORGANIZATION. — For purposes of this title, the term "entity reorganization" means the following:

(1) a mere change in the form of an entity or in its name or place of organization,

(2) a recapitalization of an entity,

(3) a combination of 2 or more entities into one entity (whether by fusion, absorption, or otherwise),

(4) a division of an entity into 2 or more entities (whether by split up, split off, spin off, or otherwise) that (immediately after the division) are under the control of the divided entity, its shareholders, or both,

(5) the acquisition of control of an entity in exchange solely for voting interests in the acquiring entity, and

(6) the acquisition of substantially all the assets of an entity in exchange solely for voting interests in the acquiring entity.

(b) CONTROL. — For purposes of this title, the term "control" means the ownership of equity interests possessing —

(1) at least 80 percent of the total combined voting power of all classes of equity interests entitled to vote, and

(2) at least 80 percent of the total number of shares of each other class of equity interests of the entity.

(c) QUALIFIED REORGANIZATION. — For purposes of this title, the term "qualified reorganization" means a reorganization of an entity pursuant to a written plan of reorganization for business (other than tax) purposes and which does not have as its purpose or effect significant avoidance of tax by any entity or shareholder.

(d) PARTY TO THE REORGANIZATION. — For purposes of this title, the term "party to the reorganization" means the following:

(1) the acquiring entity,

(2) the acquired entity,

(3) any entity resulting from the reorganization, and

(4) in the case of a reorganization resulting from the acquisition by one entity of equity interests in (or the assets of) another entity, such other entity.

(e) ACQUIRING AND ACQUIRED ENTITIES. — For purposes of this title —

(1) the term "acquiring entity" means an entity acquiring equity interests in, or assets of, another entity, and

(2) the term "acquired entity" means the entity the equity interests in which, or the assets of which, are acquired.

(f) SPECIAL RULES. — For purposes of this section, section 103, and section 104 —

(1) the tax treatment of parties to a reorganization who receive property in a liquidation that is part of the reorganization shall be dealt with under section 104 rather than section 103,

(2) a series of related transactions shall be treated as one transaction,

(3) in determining whether or not there is a qualified reorganization, a transaction's form shall be disregarded where it is inconsistent with the transaction's substance, and

(4) except to the extent provided in regulations, any entity reorganization that is not a qualified reorganization

shall be treated as a sale of the entity and of each of its assets.

SEC. 106. ADVANCE APPROVAL REQUIRED WHERE NONRESIDENT PERSON INVOLVED.

Where one or more parties to the transaction is a nonresident person, a contribution to capital, a complete liquidation, or a reorganization shall not qualify for non-recognition treatment under sections 101, 103(b)(2), or 104 (as the case may be) unless the Tax Service grants advance approval to such treatment.

CHAPTER 8
RULES RELATING TO PASS-THROUGHS

SEC. 111. INCOME DETERMINATIONS.

(a) INCOME OF PASS-THROUGH. — Determinations with respect to the income of a pass-through shall be made as if it were an individual using the accrual method of accounting, except that the following shall not be allowed to the pass-through:

(1) any deduction under section 38 for charitable contributions,

(2) any business loss carryforward under section 39, and

(3) any investment operational loss carryforward under section 40.

(b) INCOME OF MEMBER. —

(1) GENERAL RULE. — In determining the income of a member of a pass-through for the taxable year, there shall be taken into account separately such member's distributive share of each item of the pass-through's income, gain, deduction, loss, credit, charitable contributions, etc., for such year.

(2) ADDITIONAL RULES. — For purposes of paragraph (1) —

(A) each item shall be treated as distributed (whether or not distributed),

(B) each item shall retain its character, and

(C) the Tax Administrator shall by regulations provide for the grouping of items where separate statement of such items is not necessary to clearly reflect the income of the member.

(c) LIMITATION ON PASS-THROUGH OF LOSSES. —

(1) IN GENERAL. — Except in the case of a complete liquidation of a pass-through, a member shall not be allowed a deduction or loss to the extent that such allowance would reduce the member's adjusted basis in the pass-through below zero.

(2) DISALLOWANCE APPLIED PROPORTIONATELY.— The limitation of paragraph (1), shall be applied proportionately to all items of deduction and loss for the taxable year.

(3) CARRYFORWARD OF DISALLOWED ITEMS. — the disallowed portion of any item shall retain its character and be treated as an item sustained in the next taxable year.

SEC. 112. DISTRIBUTIONS BY PASS-THROUGHS.

(a) DISTRIBUTIONS IN KIND. — Any distribution in kind by a pass-through shall be treated as a sale for fair market value of the property involved and as a distribution of an amount of money equal to such fair market value.

(b) TREATMENT OF ACTUAL DISTRIBUTIONS. — Any distribution by a pass-through (including a distribution in liquidation) to a member shall be included in the member's income only to the extent it exceeds the adjusted basis of the member's interest in the pass- through. If the aggregate amount distributed in the complete liquidation of a pass-through is less than the adjusted basis of the member's interest in the pass-through, the difference shall be treated as the member's distributive share of a loss sustained by the pass-through in the taxable year in which the liquidation is completed.

SEC. 113. MEMBER'S ADJUSTED BASIS.

The adjusted basis of any member in a pass-through shall be the amount such member has contributed to the pass-through —

(1) increased by such member's distributive share of gains and other includible income,

(2) decreased by prior distributions,

(3) decreased by such member's distributive share of deductions and losses properly taken into account in determining includible income, and

(4) further adjusted (to the extent proper) for other items of the pass-through.

SEC. 114. REGULATIONS.

The Tax Administrator shall prescribe such regulations as may be necessary or appropriate to carry out this chapter, including regulations relating to —

(1) contributions to a pass-through.

(2) the treatment of liabilities for purposes of measuring contributions, distributions, and other matters,

(3) the continuation or termination of pass-throughs where there are changes in the respective interests of the members, and

(4) the treatment of the pass-through as an entity for certain purposes (such as the fringe benefit tax of section 161 and the filing of returns and auditing).

CHAPTER 9
PENSIONS

SEC. 121. TREATMENT OF QUALIFIED PENSION PLANS.

(a) EXCLUSION OF EMPLOYER CONTRIBUTIONS. — There shall be excluded from the gross income of an individual amounts contributed on the individual's behalf by the employer during the taxable year to a qualified pension plan for accumulation in the plan.

(b) DEDUCTION FOR CONTRIBUTIONS MADE BY EMPLOYEE OR BY SELF-EMPLOYED INDIVIDUAL. — An individual shall be allowed a deduction from gross income equal to the amount contributed by such individual to a qualified pension plan (whether contributed as an employee or as a self-employed individual) for accumulation in the plan.

(c) MAXIMUM AMOUNT. — In the case of an individual, the amount excluded under subsection (a), plus the amount deducted under subsection (b), shall not exceed 15 percent of the individual's earned income for the taxable year. For purposes of the preceding sentence, the term "earned income" means income subject to tax which is received or accrued from employment or self-employment.

(d) QUALIFIED PENSION PLAN NOT TAXED ON INCOME. — A qualified pension plan shall not be taxed on its income under section 1. However, any distribution from the plan shall be included in the gross income of the recipient.

(e) QUALIFIED PENSION PLAN DEFINED. — For purposes of this title, a qualified pension plan —

(1) must be formed and used exclusively for the benefit of the employee or employees for whom contributions are made and their beneficiaries,

(2) must cover at least 90 percent of all full-time employees of the employer who have completed one full year of service with the employer,

(3) must provide that the portion of the employee's share of the corpus and income of the plan shall be immediately vested in a separate account that cannot be withdrawn before the employee reaches age 55 (or, if earlier, before the employee dies),

(4) must provide for the distribution to the employee of the account over a period not more than the life expectancy of the employee or the employee and his spouse and beginning not later than the end of the year when the employee reaches age 70,

(5) must provide that if the employee dies, the balance in the employee's account in the plan will be paid to his or her beneficiaries,

(6) must provide that all corpus and income of the plan will be held in a separate legal entity, in a separate account in a bank, insurance company, or similar institution, or under a contract with an insurance company,

(7) must contain adequate safeguards against loans, sales of assets, and similar dealings between the plan and any person who participated in establishing or contributing to the plan, and

(8) must be registered under this section and must supply to the designated officer and to the employees such information as may be required by regulations.

No exclusion or deduction shall be allowed under this section unless it is established that the foregoing requirements of this subsection have been met and will continue to be met.

(f) SELF-EMPLOYED INDIVIDUALS MAY HAVE QUALIFIED PENSION PLANS. — For purposes of this section, the term "employee" includes an individual who is a proprietor, a member of a pass-through, or otherwise self-employed.

SEC. 122. FOREIGN PENSION PLANS.

(a) EXCLUSION FROM GROSS INCOME. — In the case of an employee who is a national of a foreign country and whose employment in Progresa is reasonably expected not to exceed 5 years, to the extent provided in regulations there shall be excluded from gross income contributions to, and accumulations in, a qualified foreign pension plan.

(b) QUALIFIED FOREIGN PENSION PLAN. — For purposes of subsection (a), the term "qualified foreign pension plan" means a plan determined by the Tax Administrator —

(1) to be a qualified pension plan under the laws of a foreign country, and

(2) which meets standards substantially comparable to the requirements of section 121(e).

CHAPTER 10
CROSS BORDER PROVISIONS

Subchapter A — Tax Treatment of Nonresidents

SEC. 131. TAXABLE INCOME OF NONRESIDENTS.

(a) GENERAL RULE. — In determining the taxable income of a nonresident entity or individual —

(1) only income from sources within Progresa shall be taken into account, and

(2) only expenses, losses, and other items properly allocable to the income described in paragraph (1) may be allowed as deductions.

(b) PERMANENT ESTABLISHMENTS. — In the case of a nonresident entity or individual maintaining a permanent establishment in Progresa, the permanent establishment shall be treated as a resident entity, but only with respect to income sourced within Progresa (and the expenses properly allocable thereto).

SEC. 132. GAIN WHEN INDIVIDUAL CEASES TO BE PROGRESA RESIDENT.

(a) RECOGNITION OF GAIN. — Except as provided in regulations, any individual who ceases to be a resident of Progresa shall be treated as having sold all investment and financial property at its fair market value at the time of such cessation.

(b) BASIS OF INVESTMENT AND FINANCIAL PROPERTY. — Any individual becoming a resident of Progresa may elect to establish (in the manner provided by regulations) the fair market value at such time of such individual's investment and financial property. The value so established shall be the taxpayer's basis for determining gain on the sale of such property.

(c) REGULATIONS. — The regulations under this section shall contain rules for determining —

(1) when a change in residence takes effect, and

(2) the valuation dates for purposes of subsections (a) and (b).

SEC. 133. ELIGIBILITY FOR CREDITS.

(a) WAGE WITHHOLDING. — A nonresident individual who files a return for the taxable year shall be eligible to file for a credit for amounts withheld under section 171.

(b) WITHHOLDING ON PROPERTY TRANSFERS. — A nonresident entity or individual filing a return for the taxable year shall be eligible to file for a credit for amounts withheld under section 173.

Subchapter B — Foreign Income of Progresa Residents

SEC. 136. LOOK-THROUGH IN CASE OF CERTAIN NONRESIDENT INVESTMENT ENTITIES.

(a) INCOME TAXED TO 5 PERCENT OWNERS. — The shareholder's proportionate share of the income of any nonresident entity for investing outside of Progresa shall be treated as derived directly by any 5 percent owner who is a resident taxpayer.

(b) FOREIGN TAXES PAID BY ENTITY. — For purposes of section 182, any taxpayer deriving income subject to tax by reason of subsection (a) shall be treated as having paid the foreign income taxes paid by the entity with respect to such income.

(c) ENTITY DEFINED. — For purposes of this title, the term "nonresident entity for investing outside of Progresa" means —

(1) any nonresident entity more than 50% of the income of which for the taxable year or the immediately preceding taxable year consists of foreign source investment and financial income, and

(2) any other nonresident entity formed or availed of to shield any resident person from tax under this title on foreign source investment and financial income.

(d) 5 PERCENT OWNERS. — A person shall be treated as a 5 percent owner if the equity interests of such person and all related persons equal or exceed 5 percent in value of the total equity interests in such entity.

(e) TREATMENT OF ACTUAL DISTRIBUTIONS. — A previously taxed income account shall be established for each taxpayer who has been subject to tax under subsection (a) with respect to an entity. To the extent that subsequent distributions of income to the taxpayer do not exceed the balance in such account, the taxpayer shall not be taxed with respect to such distributions.

SEC. 137. DIVIDENDS OF 10 PERCENT OWNERS FROM FOREIGN BUSINESS OPERATIONS.

If the taxpayer owns (directly or indirectly) 10 percent or more of the equity interests in a nonresident entity substantially all of the assets of which are used in the conduct of an active business outside of Progresa, then dividends received or accrued by the taxpayer from such entity shall be treated as foreign source income which is not investment and financial income.

Subchapter C — Sources of Income

SEC. 141. DIVISION OF INCOME.

(a) IN GENERAL. — All income of the taxpayer shall be divided into Progresa income and foreign income.

(b) ECONOMIC ACTIVITY TEST. — Except as otherwise provided in this title or in regulations, income shall be treated —

(1) as Progresa income, if the economic activity that produced the income took place in Progresa, and

(2) as foreign income, if the economic activity that produced the income took place in a country other than Progresa.

SEC. 142. SPECIFIC RULES FOR PROGRESA INCOME.

Except as otherwise provided in this subchapter or in regulations, the following shall be treated as Progresa income:

(1) INTEREST. — Interest on debt obligations issued by a resident entity or resident pass-through of Progresa, or by a governmental unit of Progresa,

(2) DIVIDENDS. — Dividends from a resident entity of Progresa,

(3) LABOR AND SERVICES. — Income from labor and services performed in Progresa,

(4) RENTAL INCOME. — Income from the use of movable or immovable property in Progresa,

(5) ROYALTY INCOME. — Income from the use, or the right to use, intangible property in Progresa,

(6) GAIN FROM SALE OF IMMOVABLE PROPERTY. — Gain from the sale of immovable property located in Progresa or from any other immovable property transfer described in section 173(c),

(7) GAIN FROM SALE OF MOVABLE PROPERTY. — Gain from the sale of movable property (other than inventory) where the seller is a resident of Progresa, and

(8) INSURANCE PREMIUMS. — The premiums for insuring or reinsuring Progresa risks (as defined in regulations).

SEC. 143. SPECIFIC RULES FOR FOREIGN INCOME.

For purposes of determining foreign income, section 142 shall be reapplied by substituting "a country other than Progresa" for "Progresa" each place it appears in section 142.

SEC. 144. ADDITIONAL RULES.

(a) INSUFFICIENT REFLECTION OF PROGRESA INCOME. — Where under the foregoing rules the income from Progresa is not clearly reflected, the division of income between Progresa income and foreign income shall be determined by the designated tax officer in the manner provided by regulations.

(b) DEDUCTIONS. — For purposes of this title, a deduction shall be allocated to the income (Progresa or foreign) in the production of which the deduction was incurred.

SEC. 146. TAX TREATIES.

If any provision of this Code contravenes any provision of a tax treaty entered into by Progresa, the provision of the tax treaty shall prevail.

CHAPTER 11
SPECIAL PROVISIONS

SEC. 151. BAD DEBT RESERVE FOR BANKS.

(a) ESTABLISHMENT OF BAD DEBT RESERVE. — Any bank or similar financial institution established and operated in accordance with law may establish and maintain a reserve to which all losses on loans are charged.

(b) EXPERIENCE METHOD USED. — Any reserve described in subsection (a) shall be based on the experience of the financial institution and of similar financial institutions in the manner prescribed by regulations and shall not exceed a percentage of the loans prescribed in such regulations.

(c) TREATMENT OF ADDITIONS AND SUBTRACTIONS. — Any net addition to a reserve described in subsection (a) shall be allowed as a deduction. Any net reduction in such a reserve shall be included in income.

SEC. 152. TREATMENT OF INSURANCE COMPANIES.

(a) AMOUNT OF TAX. — In the case of an entity whose principal activity is the insurance or reinsurance of life, property, or other risks, the tax imposed by section 1 for any taxable year shall be an amount equal to 10 percent of the gross premiums accrued during the year for insurance or reinsurance of Progresa risks (as defined in regulations).

(b) TREATMENT OF NONINSURANCE ACTIVITIES. — In the case of an entity described in subsection (a), all its activities other than insur-

ance and reinsurance shall be treated as the activities of an entity that is not an insurance company.

CHAPTER 12
RELATED TAXES

SEC. 161. FRINGE BENEFIT TAX.

(a) TAX IMPOSED. — There is hereby imposed on any fringe benefit furnished by an employer a fringe benefit tax. The tax shall equal 30 percent of the grossed up amount of the fringe benefit.

(b) GROSSED UP AMOUNT OF FRINGE BENEFIT. — The amount taken into account for any fringe benefit under this section shall be —

(1) its fair market value (as determined under regulations), divided by

(2) 0.70.

(c) MEANING OF EMPLOYER. — For purposes of this section and section 162 —

(1) PERSONS ACTING FOR EMPLOYERS. — The furnishing of a benefit by a third person on behalf of the employer shall be treated as a benefit furnished by the employer.

(2) CERTAIN INDEPENDENT CONTRACTORS. — The furnishing of a benefit to an individual who is supplying goods or services to a business (other than in an employment relationship) shall, to the extent provided in regulations, be treated as a furnishing to an employee of such business.

(d) EMPLOYER LIABLE FOR TAX. — Each employer furnishing fringe benefits during any month shall pool together all fringe benefits and shall be liable for the tax on such benefits.

(e) MONTHLY RETURNS AND PAYMENTS. — The tax imposed by subsection (a) shall be declared on a form prescribed by regulations and shall be paid on a monthly basis.

SEC. 162. FRINGE BENEFIT DEFINED.

(a) IN GENERAL. — For purposes of this title, the term "fringe benefit" means any good, service, or other benefit furnished in cash or kind by an employer to an individual in respect of an employment relationship, but only if such benefit includes a substantial personal element in addition to the employment related element.

(b) BENEFITS SPECIFICALLY INCLUDED. — The benefits to which subsection (a) applies shall include (but not be limited to) the furnishing of —

(1) a vehicle of any kind,

(2) food,

(3) housing,

(4) household personnel,

(5) a loan at less than market rate,

(6) a discount on the sale of goods,

(7) educational assistance for the public official or employee and dependents (not including training programs

directly related to the performance of the duties of the public official or of the employee),

(8) life and health insurance premiums and similar amounts,

(9) an expense allowance, except to the extent it is substantiated that the expense (and the amount thereof) was reasonable and necessary to the business of the employer, and

(10) contributions to social security plans, to the extent that these contributions exceed the standard levels fixed by law.

(c) BENEFITS EXCLUDED. — The term "fringe benefit" does not include —

(1) any cash payment of a kind ordinarily treated as salary, wages, or other compensation for services, and

(2) any pension contribution excluded from the income of the recipient under section 121 or 122.

(d) ENTERTAINMENT, AMUSEMENT, AND RECREATION. — For purposes of this title, the term "fringe benefit" includes the furnishing of entertainment, amusement, or recreation (or facility therefor) whether or not the furnishing takes place in an employment relation. The preceding sentence shall not apply to the business of furnishing entertainment, amusement, or recreation (or facility therefor).

SEC. 163. INTEREST PAID TO RESIDENT INDIVIDUALS BY RESIDENT FINANCIAL INSTITUTIONS.

(a) TAX IMPOSED. — There is hereby imposed on any interest paid by a resident financial institution to a resident individual a tax equal to 5 percent of the amount before tax.

(b) INTEREST COVERED. — Subsection (a) applies to interest paid directly or through a broker, agent, or other intermediary or through a pass-through.

(c) NO SECTION 1 TAX ON THIS INTEREST. — For exclusion from gross income of interest taxable under subsection (a), see section 13(c)(8).

SEC. 164. ADVANCE TAX ON DIVIDEND DISTRIBUTIONS.

(a) ADVANCE TAX ON THE INCOME OF ENTITIES. — If an entity distributes dividends to its shareholders during the taxable year, it shall withhold (and pay as tax) an amount equal to 30 percent of the amount the dividend would be if there was no withholding.

(b) ENTITY ALLOWED CREDIT AGAINST ITS INCOME TAX. — If any entity withholds any amount under subsection (a), such amount shall be a credit against the tax imposed by section 1 on the distributing entity's taxable income for the taxable year in which the withholding takes place. No credit shall be allowed to an insurance company against its section 1 tax determined under section 152 on its gross premiums instead of its taxable income.

(c) TREATMENT OF EXCESS CREDITS. — If for any taxable year the credit allowable to an entity under subsection (b) exceeds the entity's tax under section 1 for such year, such excess shall be carried forward and shall be a credit for the year following the year in which it arose.

(d) DIVIDENDS WHERE THERE IS DIRECT INVESTMENT. — Each entity (hereinafter called "first entity") owning 20 percent or more in value of the equity in a second entity shall establish a dividend account. Whenever the first entity receives a dividend from the second entity it shall exclude the net amount it receives from gross income but shall add such net amount to its dividend account. Subsequent dividends by the first entity to its shareholders shall be made first out of the dividend account to the extent thereof and shall not be subject to withholding under subsection (a).

(e) SHAREHOLDERS EXCLUDE DIVIDENDS. — An individual or entity receiving a dividend from an entity required to withhold on such dividend under subsection (a) or a dividend from a dividend account described in subsection (d) shall not include such dividend in income.

CHAPTER 13
WITHHOLDING TAXES AND ADVANCE PAYMENT OF TAX

SEC. 171. WAGE WITHHOLDING.

(a) GENERAL RULE. — Every resident payor paying wages to an employee shall withhold from such wages a tax determined under this section.

(b) EMPLOYERS WHO ARE NOT PRINCIPAL EMPLOYERS. — If the payor is not the employee's principal employer, the amount withheld shall be 30 percent of the wages (before withholding).

(c) PRINCIPAL EMPLOYER. — The amount withheld from wages by a principal employer shall be determined under withholding tables for the appropriate payroll period. Such tables —

(1) shall be based on a basic amount for each bracket, determined by dividing the bracket amounts set forth in section 3(a) by the number of payroll periods in a calendar year,

(2) shall assign one basic amount to each bracket for the first payroll period of the calendar year,

(3) shall assign one additional basic amount to each bracket for each payroll period after the first,

(4) shall compute a tentative tax on the cumulative wages paid by the principal employer during the year and on or before the last day of the payroll period, and shall

reduce this tentative tax by the sum of the amounts withheld by the principal employer for prior payroll periods in the year, and

(5) shall provide that refund of overwithholding by the principal employer shall be made not earlier than with respect to the determination of the tax due for the last payroll period in the calendar year.

(d) MONTHLY TABLES FOR PRINCIPAL EMPLOYERS. — The tables prescribed under subsection (c) for payroll periods consisting of calendar months shall be constructed as follows:

(1) The basic monthly amount for the zero bracket shall be wages from PR zero through PR 4167. The basic monthly amount for the 15% bracket shall be wages from PR 4167 through PR 8333. The basic monthly amount for the 30% bracket shall be wages over PR 8333.

(2) Table for January. —

Wages —	**Tax Due —**
Not over PR 4167	Zero
PR 4167-8333	15% of excess over PR 4167
Over PR 8333	PR 625 plus 30% of excess over PR 8333

(3) Table for February. —

Wages —	**Tax Due —**
Not over PR 8333	Zero
PR 8333-16667	15% of excess over PR 8333
Over PR 16667	PR 1250 plus 30% of excess over PR 16667

(4) Table for March. —

Wages —	**Tax Due —**
Not over PR 12,500	Zero
PR 12,500-25,000	15% of excess over PR 12,500
Over PR 25,000	PR 1875 plus 30% of excess over PR 25,000

(5) Tables for April and subsequent months. — The tables for April and subsequent months shall be determined by adding one additional basic monthly amount to each bracket for each such subsequent month.

(6) Credit for prior month taxes. — In the case of each month after January there shall be credited against the tax determined under the month's table with respect to cumulative wages the sum of the taxes withheld by the principal employer for prior months in the calendar year. No refund of any overpayment of monthly withholding under these tables shall be made before the settlement of tax due for December.

(e) INDIVIDUAL MAY HAVE ONLY ONE PRINCIPAL EMPLOYER AT A TIME. — An individual may have only one principal employer at a time. This shall be the employer designated by the employee at the time and in the manner provided by regulations. An individual may designate one or more successor principal employers during the calendar year, but only if the individual's wage and withholding records of prior principal employers during the calendar year are transferred (in the manner provided by regulations) to the new employer.

(f) PAYROLL PERIODS. — For purposes of this section, the term "payroll period" means a period for which a payment of wages is ordinarily made to the employee by the employer. Such period may be any one or more of the following specified in regulations: daily, weekly, biweekly, semimonthly, monthly, quarterly, semiannual, annual, or miscellaneous.

(g) WAGES DEFINED. — For purposes of this chapter, the term "wages" means any of the following amounts paid by an employer in cash or in kind —

(1) wages, salaries, and bonuses, and

(2) to the extent provided in regulations, any other compensation.

(h) AMOUNTS EXCLUDED FROM WAGES. — For purposes of this chapter, the term "wages" does not include —

(1) any compensation excluded from gross income under section 13(c) or any other provision of this Code, and

(2) any income from sources outside of Progresa.

(i) RESIDENT PAYOR. — For purposes of this chapter, the term "resident payor" means —

(1) any resident entity or pass-through,

(2) any permanent establishment in Progresa of a nonresident person,

(3) any governmental unit or nonprofit organization described in section 91(b), and

(4) any resident individual, but only with respect to payments by such individual in carrying on a business.

(j) EMPLOYEE. — For purposes of this section —

(1) OFFICERS AND DIRECTORS INCLUDED. — The term "employee" includes any governmental officer (including an elected official) and the officer or director of any entity.

(2) CERTAIN INDEPENDENT CONTRACTORS. — To the extent provided in regulations, income from the performance of services by an individual who is not called an employee but who has two or more of the significant char-

acteristics of an employee (as set forth in the regulations) shall be treated as wages paid to an employee.

(k) WAGE WITHHOLDING TREATED AS FINAL TAX IN CERTAIN CASES. — If —

(1) a resident individual has no gross income for the taxable year other than wages subject to withholding under this section and interest described in section 163, and

(2) the taxpayer does not elect to file a return for the taxable year,

then the tax so withheld shall constitute the taxpayer's final section 1 tax for such year.

SEC. 172. WITHHOLDING ON INTEREST, ROYALTIES, AND GAMBLING WINNINGS.

(a) TAX IMPOSED. — Any resident payor (within the meaning of section 171(i)) making any payment described in subsection (b) to or for the benefit of any person shall withhold from the payment and pay as tax an amount equal to the percent of the payment (before withholding) determined under subsection (c).

(b) PAYMENTS SUBJECT TO WITHHOLDING UNDER THIS SECTION. — The payments described in this section are payments constituting income from sources within Progresa that are —

(1) interest,

(2) royalties, or

(3) lottery or other gambling winnings.

(c) RATE OF WITHHOLDING. — The rate of withholding under this section shall be the following percent of the payment (before withholding):

Type of Payment	Percent
Interest described in section 163	5
Other interest	15
Royalties	15
Lottery or other gambling winnings	30

(d) TAX TREATED AS FINAL TAX FOR NONRESIDENT PERSONS. — In the case of a nonresident person, the tax imposed by this section shall constitute the final section 1 tax on the withheld amounts.

SEC. 173. WITHHOLDING ON TRANSFERS OF INTERESTS IN PROGRESA IMMOVABLE PROPERTY.

(a) WITHHOLDING. — To the extent provided in regulations, any person making any payment in connection with a Progresa immovable property transfer shall withhold from the payment, and pay as tax, the amount described in subsection (b).

(b) AMOUNT WITHHELD. — The amount described in this subsection is the lesser of —

(1) 15 percent of the payment (before withholding),

or

(2) 30 percent of the transferor's gain.

For purposes of paragraph (2), the person making the payment may rely on a certification of the transferor's gain that conforms to the requirements prescribed by regulations.

(c) PROGRESA IMMOVABLE PROPERTY TRANSFER. — For purposes of this section, the term "Progresa immovable property transfer" means the transfer of any interest in immovable property situated in Progresa. Such term includes the transfer of an equity interest in an entity 50 percent or more of the holdings of which consists of direct or indirect interests in Progresa immovable property.

SEC. 174. WITHHOLDING ON PAYMENTS TO NONRESIDENT INDIVIDUALS AND ENTITIES.

(a) WITHHOLDING. — A resident payor (within the meaning of section 171(i) making any payment of income from Progresa sources (other than a payment described in subsection (b)) to a nonresident individual or nonresident entity shall withhold from the payment, and pay as tax, an amount equal to 15 percent of the payment (before withholding).

(b) SECTION NOT APPLICABLE TO CERTAIN AMOUNTS. — This section shall not apply to —

(1) wages (as defined in section 171(g)),

(2) interest and royalties,

(3) lottery and other gambling winnings,

(4) payments in connection with the transfer of immovable property, and

(5) dividends excluded under section 164(e).

(c) TAX TREATED AS FINAL TAX. — The tax imposed by this section shall constitute the final section 1 tax on the withheld amounts.

SEC. 175. ADVANCE PAYMENT OF INCOME TAX.

(a) REQUIREMENT OF PAYMENT. — Except as provided by regulations, every person shall pay an advance tax equal to 100 percent of such person's tax under section 1 for the preceding year. Such payment shall be in 3 installments as follows:

On or before the following dates in the current year:	**Percentage of advance tax due:**
June 30	50 percent
September 30	30 percent
December 31	20 percent

(b) REDUCTION FOR WITHHELD AMOUNTS. — The amount treated as the advance tax due for the current year shall be reduced by the aggregate amount withheld under sections 171, 172, and 173, and allowable as a credit against the tax imposed by section 1 for the current year.

(c) TAXPAYER WITH LOWER INCOME. — A taxpayer who can demonstrate that the income for the current year is at least 30 percent less than the income for the preceding year may request, at least one month in advance of an installment payment date set forth in subsection (a), that the remaining installments be reduced. The designated officer

may excuse the taxpayer in whole or in part from the requirement of paying such installments.

(d) UNDERPAYMENTS. — Any underpayment of an installment required by this section shall bear interest, at the rate provided in section 561(c), from the installment due date to the due date for the return for the current year of the tax imposed by section 1.

CHAPTER 14
CREDITS

SEC. 181. CREDITS AGAINST TAX.

(a) CREDITS AGAINST SECTION 1 TAX. — Taxpayers may credit against the tax imposed by section 1 for the taxable year the following amounts:

(1) amounts withheld during the same taxable year under section 171, 172, or 173,

(2) advance payments during the same taxable year under section 175, and

(3) foreign tax credits allowable under section 182 for amounts paid or accrued and allocated to the same taxable year.

(b) TREATMENT OF CREDIT BALANCE. — For treatment of credit balance where a taxpayer's credits against tax exceed the amount of such tax, see section 523(a).

SEC. 182. CREDIT FOR FOREIGN TAX ON INVESTMENT AND FINANCIAL INCOME.

(a) ALLOWANCE OF CREDIT. — A taxpayer may elect to credit against the section 1 tax income taxes paid to any foreign country in which investment and financial income arises if such income is also subject to the section 1 tax. A taxpayer who elects to credit any income tax of a foreign country under this section for any taxable year may

not claim a deduction of any income tax of such foreign country for such year.

(b) PER COUNTRY LIMITATION. — The amount of the credit with respect to income taxes paid to any foreign country for any taxable year shall not exceed the proportion of the taxpayer's total section 1 liability for such year that the gross investment and financial income of the taxpayer from sources within the foreign country (less expenses attributable to earning such gross income) for such period bears to the taxpayer's total taxable income for such year.

(c) YEAR OF CREDIT. — A tax paid to a foreign country shall be creditable for the year for which the income is taxable under section 1.

(d) FOREIGN COUNTRY INCLUDES POLITICAL SUBDIVISIONS. — For purposes of this section, the term "foreign country" includes a political subdivision of such country.